

General Information Letter: Response to questions regarding income taxation and withholding requirements for compensation paid to players, managers, and other employees of professional sports teams and to musicians and other entertainers.

January 26, 1998

Dear:

This is in response to your letter dated January 15, 1998 in which you request information concerning Illinois taxation of non-resident professional athletes. Department rules require that the Department issue two types of letter rulings, private letter rulings (PLRs) and general information letters (GILs). For your general information, please find enclosed herewith a copy of 2 *Ill. Adm. Code 1200* regarding letter rulings and other information issued by the Department.

Although you have not specifically requested either type of ruling, the nature of your questions and the information you have provided require that I respond with a GIL. GILs are designed to provide background information on specific topics. However, general information letters are not rulings that are binding on the Department.

In your letter you have stated in part as follows:

Please provide information and documentation on Illinois withholding requirements for the following categories of professionals and entertainers,

1. Non-resident professional team athletes (including coaches, managers, and trainers) who perform services in Illinois;
2. Non-resident professional athletes who are not team members (golfers, boxers, etc.) performing services in Illinois;
3. Non-resident entertainers (actors, musicians, etc.) performing services in Illinois.

If no special provisions apply, please sign below to acknowledge the accuracy of the following statement.

All wages earned by an employee in Illinois are subject to Illinois' withholding tax. There are no special provisions for taxing professional athletes and entertainers. Illinois withholding is determined by using the withholding tables or percentage formula. No documentation is available.

If the above information is not correct, please furnish a copy of the documentation that would substantiate the correct information.

For your information, *Illinois Income Tax Act (IITA) Section 301* provides the general rules with respect to allocation of income received by residents. *IITA Section 301(a)* provides that "all items of income or deduction which were taken into account in the computation of base income for the taxable year by a resident shall be allocated to this State." *IITA Section 301(c)* states

(c) Other persons.

(1) In general. Any item of income or deduction which was taken into account in the computation of base income for the taxable year by any person other than a resident and which is referred to in Section 302, 303, or 304 (relating to compensation, nonbusiness income and business income, respectively) shall be allocated to this State only to the extent provided by such section.

(2) Unspecified items. Any item of income or deduction which was taken into account in the computation of base income for the taxable year by any person other than a resident and which is not otherwise specifically allocated or apportioned pursuant to Section 302, 303 or 304 (including, without limitation, interest, dividends, items taken into account under the provisions of Sections 401 through 425 of the Internal Revenue Code, and benefit payments received by a beneficiary of a supplemental unemployment benefit trust which is referred to in Section 501(c)(17) of the Internal Revenue Code):

(A) in the case of an individual, trust or estate, shall not be allocated to this State; and

(B) in the case of a corporation or a partnership, shall be allocated to this State if the taxpayer had its commercial domicile in this State at the time such item was paid, incurred or accrued.

With respect to compensation (i.e., wage income) paid to a nonresident, *IITA Section 302(a)* provides that "[a]ll items of compensation paid in this State (as determined under *IITA Section 304(a)(2)(B)*) to an individual who is a nonresident at the time of such payment and all items of deduction directly allocable thereto, shall be allocated to this State." According to *IITA Sec. 302(a)(2)(B)*, compensation is "paid in this State" if:

(i) The individual's service is performed entirely within this State;

(ii) The individual's service is performed both within and without this State, but the service performed without this State is incidental to the individual's service performed within this State; or

(iii) Some of the service is performed within this State and either the base of operations, or if there is no base of operations, the place from which the service is directed or controlled is within this State, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this State. Beginning with taxable years ending on or after December 31, 1992, for residents of states that impose a comparable tax liability on residents of this State, for purposes of item (i) of this paragraph (B), in the case of persons who perform personal services

under personal service contracts for sports performances, services by that person at a sporting event taking place in Illinois shall be deemed to be a performance entirely within this State. (emphasis added).

Except for the underlined sentences, the foregoing rules will govern whether the attribution of wages paid to non-resident employees. This would include nonresident managers, coaches, trainers, and other entertainers on salary. By contrast, the highlighted language specifically covers compensation income paid to nonresident athletes who are employed by out-of-state teams. As you can see, the Illinois law governing the taxation of such income is retaliatory in nature. If the athlete is a member of team located in a state that taxes players from Illinois teams when the Illinois team plays in that state, then Illinois will impose a tax on players on teams from that state when they play in Illinois. The Department has adopted rules on the retaliatory tax. Please see *IIT Regulation Sections 100.3100(e) and 100.3120(a)(3)(A)*, copies enclosed.

Individual, non-resident athletes (e.g., golfers, tennis players) and entertainers (e.g., band members and other performing artists) are also potentially subject to Illinois income tax on non-wage income (i.e., income other than from "compensation"). As mentioned under *IITA Sec. 301(c)(1)* above, non-wage income includes non-business income, which is governed by *IITA Sec. 303* and business income, which is governed by *IITA Section 304*.

Non-business income is allocated under *IITA Section 303* by rules which are specific to the type of income involved (e.g., rents, royalties, and capital gains). Under *IITA Section 304* however, the non-resident's business income is subject to Illinois state income taxation under a three-factor formula. That formula multiplies business income by a fraction, the numerator of which is Illinois property, payroll, and double-weighted sales and the denominator of which is property, payroll, and double-weighted sales throughout the United States

For your information, in the case of non-resident individuals who have incorporated themselves and who derive income from Illinois activities, please be advised that corporations are not residents of Illinois. *IITA Section 1501(a)(20)*. Thus, their business and non-business income will be allocated and apportioned in the same manner as that of non-resident individuals.

With respect to withholding, *IITA Section 701(a)* sets forth the basic *IITA* withholding requirements with respect to Illinois income tax withholding. This section provides in pertinent part that if withholding on compensation is required for federal income tax purposes, it will also be required for Illinois income tax purposes. In general, employers maintaining an office or transacting business within this State are required to withhold Illinois income tax on compensation paid in this state. *86 Ill. Adm. Code 100.7010* (copy enclosed). That rule provides guidance for determining when compensation is paid in this State, and is therefore subject to withholding. However, if the employer is not required to withhold federal income tax because of the provisions of federal law or a federal treaty, the employer will also not be required to withhold Illinois income tax.

Please be also advised that any entity that has employees subject to income tax withholding must register and withhold income taxes, whether that entity is for profit or not-for-profit. **Form NUC-1**, copy enclosed, must be filed with the Department in order to meet this registration requirement.

We enclose herewith the **Il-700 Booklet (Illinois Withholding Tax Guide and Tables)**, which details the aforementioned Illinois income tax withholding requirements. The enclosed **Booklet** summarizes and describes filing requirements, procedures, and forms required of employers. On pages 6 and 7 you will find detailed information in regard to the filing of **Forms W-2**, magnetic filing, and other required forms relating to the withholding of Illinois income tax. Page 9 of this **Booklet** contains copies and **Forms IL-501, IL-941, and IL-W- 3**, and describes attachments and remittances required.

Section 100.7010(a) of the Department's rules provides in pertinent part that "Illinois will recognize reciprocal withholding exemption agreements for those individuals subject to withholding by virtue of P.A. 87-880 [the statute enacting retaliatory tax on pro athletes], to the extent that the state of residence of the team by which they are employed recognizes the reciprocal withholding exemption agreement with respect to individuals employed by teams with Illinois residence."

We enclose herewith a copy of the *IITA* and the *IIT Regulations* for your reference.

As we noted above, the foregoing discussion is a GIL and not a PLR. In order to request a PLR, it would be necessary to provide us with a request that complies with the requirements of *IIT Reg. Sec. 1200.110* of our rules.

Very truly yours,

Jackson E. Donley,
Associate Counsel (Income Tax)